Nos. 14-1513 & 14-1520

IN THE

Supreme Court of the United States

HALO ELECTRONICS, INC.,
Petitioner,

v.

PULSE ELECTRONICS, INC., ET AL.,
Respondents.

STRYKER CORPORATION, ET AL.,
Petitioners,

v.

ZIMMER, INC., ET AL.,
Respondents.

On Writs of Certiorari to the United States Court of Appeals for the Federal Circuit

BRIEF OF *AMICUS CURIAE* HUAWEI TECHNOLOGIES CO., LTD. SUPPORTING RESPONDENTS

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QUESTION PRESENTED

Whether damages in a patent infringement case may be trebled under 35 U.S.C. § 284, even though the defendant presents objectively reasonable defenses that the patent-in-suit is invalid or not infringed.

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BRIEF OF *AMICUS CURIAE* HUAWEI TECHNOLOGIES CO., LTD. SUPPORTING RESPONDENTS

INTEREST OF *AMICUS CURIAE*[1]

[1] All counsel of record, with the exception of counsel for Zimmer, Inc., consented to the filing of this brief by filing blanket consents with the Clerk. Counsel of record for Zimmer has consented to the filing of this brief. *Amicus* states that no portion of this brief was authored by counsel for a party and that no person or entity other than *amicus* or their counsel made a monetary contribution intended to fund the preparation or submission of this brief.

Huawei Technologies Co., Ltd. is the world's second largest manufacturer of cellular network infrastructure equipment and applies for more patents than any other company in the world.[2] Headquartered in Shenzhen, China, with principal U.S. offices in Texas and California, its products serve over one-third of the world's population. Huawei ranks among the top five mobile handset vendors worldwide. Huawei's telecom network equipment, IT products and solutions, and smart devices can be found in 170 countries and regions. In 2014, Huawei achieved $46.7 billion in annual sales revenue, ranking it 228th in the Global Fortune 500.

Innovation is at the core of Huawei's business. Huawei consistently invests over 10% of its annual revenue in research and development. In 2014, for example, Huawei invested $6.6 billion (14.2% of its total 2014 revenue) in developing new products for the marketplace. This research and development spans the globe, with significant research activities occurring in many countries, including a $1.1 billion presence in the United States.

This commitment to innovation has resulted in Huawei holding one of the largest patent portfolios in the world, consisting of over 41,000 patents. This number grows each year as Huawei continues to pursue new inventions, applying for over 4,000 new patents each year. In 2014, for instance, Huawei and its subsidiaries received over 1,000 new patents in the United States alone, ranking it among the top 30 companies in securing U.S. patents.[3]

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[2] World Intellectual Property Organization, Who Filed the Most PCT Patent Applications in 2014?, http://www.wipo.int/export/sites/www/ipstats/en/docs/infographics_pct_2014.pdf.

[3] U.S. Patent and Trademark Office, Patenting by Organization (Utility Patents) 2014, http://www.uspto.gov/web/offices/ac/ido/oeip/taf/topo_14.htm.

As evidenced by its robust patent program, Huawei believes that protection of intellectual property is of utmost importance both to its business and to the telecommunications industry as a whole. Huawei seeks to maintain a legal environment that protects research investment and rewards innovation, while at the same time allowing for healthy competition. Huawei's licensing policy reflects that approach, as Huawei has executed licensing agreements allowing many of its competitors to use Huawei's U.S.-patented innovations.

Huawei has a strong interest in this case because its drive to innovate and compete in the marketplace inevitably gives rise to patent-infringement disputes with other intellectual-property holders and competitors. Particularly pernicious are the often baseless infringement claims asserted by non-practicing entities (NPEs). NPE litigation represents a serious threat to Huawei's continued innovation. Huawei is a favorite target of NPEs. In 2013, Huawei was one of the top 10 companies most often sued by NPEs.[4] And in the last year alone, Huawei spent tens of millions of dollars defending NPE lawsuits. That amount exceeds both Huawei's profits from the U.S. market and the operating costs of its U.S. subsidiaries.

Huawei is concerned about the disastrous effects on high-tech companies that would result if this Court rejects the *Seagate* test or otherwise loosens the strictures on the award of enhanced damages. The threat of infringement suits already imposes steep costs on innovating companies, and allowing district courts to impose treble damages guided only by their discretion would increase those costs even further. The very real prospect of treble damages in run-of-the-mill infringement suits

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[4] RPX Corp. 2013 NPE Litigation Report 30 (2014), https://www.rpxcorp.com/wp-content/uploads/2014/01/RPX-2013-NPE-Litigation-Report.pdf.

would force high-tech companies to settle even marginal claims in order to avoid the risk of enormous judgments. And the greatest beneficiaries of this new rule would be NPEs, entities who have no fear of infringement suits because they do not engage in innovation, much less market products.

That is not to say that Huawei opposes enhanced damages in every instance. As one of the largest patent holders in the world, Huawei knows all too well the need to discourage anti-competitive behavior in the intellectual-property context. Without the threat of enhanced damages, some operating companies (whether direct competitors or competitors of the patentee's customers) could brazenly resist reasonable licensing negotiations in favor of simply copying the innovation and daring the patent holder to undergo the costly exercise of bringing suit. That lawsuit would normally result in damages equal to the licensing fees they would have otherwise paid (and perhaps attorney's fees in exceptional cases). Thus, without enhanced damages, direct competitors and competitors of the patentee's customers have little to lose and much to gain by deliberately infringing. Yet the patent holder's business suffers irreparable harm as a result of each instance of this unfair competition, harm that compensatory damages cannot cure. For a large patent holder like Huawei, this process must be repeated virtually *ad infinitum*, with each case piling more expenses and competitive harm on the patent holder. Enhanced damages can deter such unfair competition and send a strong message that indefensible, bad-faith efforts to inflict competitive harm will be punished.

In sum, Huawei seeks to ensure that U.S. patent law continues to safeguard innovation by imposing suitably stringent requirements on the award of enhanced damages, particularly in suits brought by NPEs, while at the

same time preserving enhanced damages as a strong deterrent to egregiously unfair competitive behavior.

SUMMARY OF ARGUMENT

Outside the patent context, this Court imposes strict limitations on punitive damages in order to control that powerful sanction and ensure that courts deploy it only in extreme cases of egregious conduct. Similar constraints should govern the award of enhanced damages under Section 284, which this Court has recognized as a species of punitive damages. Indeed, the unique characteristics of the patent-infringement context heighten the need for such limitations on punitive awards. Pernicious NPE litigation is already threatening continued innovation. Arming NPEs with the increased ability to credibly demand treble damages will accelerate this disturbing trend. More generally, loosening the test for treble damages risks deterring beneficial innovative behavior and chilling challenges to questionably valid patents.

To be sure, enhanced damages have a place in patent law. They fulfill a necessary, targeted role: to deter the worst kind of infringement, such as a company copying a product from a competitor without any legal basis or refusing to engage in good-faith licensing negotiations despite a patent's clear validity. Without the threat of enhanced damages, these types of infringement would impose heavy costs on patent holders at little risk to the infringer. In such circumstances, damages must be more than the royalty that would have otherwise been paid if the law is to deter this bad-faith and baseless infringement. The lessons of punitive-damages law may be usefully employed to cabin enhanced damages to their proper, limited sphere.

ARGUMENT

I. BECAUSE ENHANCED DAMAGES UNDER SECTION 284 ARE A SPECIES OF PUNITIVE DAMAGES, THE GOVERNING TEST MUST ENSURE THEY REMAIN A RARE EXCEPTION FOR THE MOST EGREGIOUS CASES.

A. This Court has long held that enhanced damages under Section 284 are a type of punitive damages.

As the Government acknowledges, this Court has long recognized that enhanced damages for patent infringement are a form of punitive damages. See United States Br. 13, 16-17. As early as 1853, this Court held under the Patent Act of 1836 that "trebling the actual damages found by the jury" constitutes "vindictive or punitive damages." *Seymour* v. *McCormick*, 57 U.S. 480, 489 (1853). The Court repeated that view a few decades later when it emphasized that enhanced infringement damages are "vindictive or punitive damages." *Tilghman* v. *Proctor*, 125 U.S. 136, 144 (1888). The 1952 recodification did not change the nature of enhanced damages, with the Court continuing to reference the "punitive or 'increased' damages under the statute's trebling provision." *Aro Mfg. Co.* v. *Convertible Top Replacement Co.*, 377 U.S. 476, 508 (1964). In recent years, this Court reaffirmed that approach, classifying Section 284 enhanced damages as "punitive damages." *Florida Prepaid Postsecondary Educ. Expense Bd.* v. *Coll. Sav. Bank*, 527 U.S. 627, 648 n.11 (1999).

That settled framework makes sense. This Court has known since the Patent Act of 1836 that Congress did not intend to treble actual damages for ordinary infringers: "For there is no good reason why taking a man's property in an invention should be trebly punished, while the measure of damages as to other property is single and actual damages." *Seymour*, 57 U.S. at 488-489. Indeed,

an animating purpose of the 1836 Act was to "obviate th[e] injustice" created by the prior statute, which imposed treble damages on all infringers rather than only on those deserving punishment. *Ibid.* Under the 1836 Act and current law, therefore, the enhanced-damages provision may be used only "to punish the defendant" for truly egregious conduct, *id.* at 489, not to reward successful plaintiffs.

B. As with all punitive damages, the law must ensure that enhanced damages under Section 284 are awarded rarely and only in extreme cases.

1. *Punitive damages and enhanced damages under Section 284 are reserved for the worst conduct.*

As a species of punitive damages, enhanced damages under Section 284 must be rare and awarded only to penalize and deter outrageous conduct: "The prevailing rule in American courts * * * limits punitive damages to cases of * * * 'enormity,' where a defendant's conduct is 'outrageous,' owing to 'gross negligence,' 'willful, wanton, and reckless indifference for the rights of others,' or behavior even more deplorable." *Exxon Shipping Co.* v. *Baker*, 554 U.S. 471, 493 (2008). This high threshold exists because punitive damages are "intended to punish the defendant and to deter future wrongdoing" in extreme cases. *Cooper Indus., Inc.* v. *Leatherman Tool Grp., Inc.*, 532 U.S. 424, 432 (2001). Accord *State Farm Mut. Auto. Ins. Co.* v. *Campbell*, 538 U.S. 408, 416 (2003) ("[P]unitive damages * * * are aimed at deterrence and retribution.").

This Court has likewise taken similar measures to limit enhanced damages to the rare, appropriate cases in the Section 284 context. It has restricted their award to cases of "wanton and malicious" conduct, *Seymour*, 57 U.S. at 488, or "willful or bad-faith infringement," *Aro*, 377

U.S. at 508, both attempts to ensure that courts may impose that harsh sanction only on particularly blameworthy infringers. The Court's more recent punitive-damages case law provides a valuable aid in fleshing out these dicta to channel the discretion of courts in a way that deters the most egregious infringing conduct, without chilling innovation that sometimes requires testing the boundaries of old and vague patents.

2. *Enhanced damages are commonly awarded even under the* Seagate *test, cautioning against further weakening that standard.*

An analysis of empirical data on the prevalence of enhanced-damages awards under *Seagate* and its predecessor test provide the Court with a useful perspective as it ensures that enhanced damages under Section 284 remain—like other forms of punitive damages—a rare exception. In *Seagate*, the Federal Circuit reaffirmed its rule that "an award of enhanced damages requires a showing of willful infringement." *In re Seagate Tech., LLC*, 497 F.3d 1360, 1368 (Fed. Cir. 2007). It then turned to defining willfulness in a manner that would give meaningful guidance to the fact finders who decide that issue. *Id.* at 1370-1372. Recognizing that its prior willfulness test set a "lower threshold for willful infringement that is more akin to negligence" and thus "allow[ed] for punitive damages in a manner inconsistent with Supreme Court precedent," the court adopted a new, more vigorous willfulness standard to cabin the award of enhanced damages to their proper sphere. *Id.* at 1371.

Under this new standard, the patent holder must satisfy a two-part test to demonstrate willfulness. First, "a patentee must show by clear and convincing evidence that the infringer acted despite an objectively high likelihood that its actions constituted infringement of a valid patent." *Ibid.* Second, "the patentee must also demonstrate that this objectively-defined risk * * * was either

known or so obvious that it should have been known to the accused infringer." *Ibid.* After an initial finding of willfulness, the judge decides whether and in what amount to award enhanced damages by applying the various factors discussed in *Read Corp.* v. *Portec, Inc.*, 970 F.2d 816, 827 (Fed. Cir. 1992). *Spectralytics, Inc.* v. *Cordis Corp.*, 649 F.3d 1336, 1348 (Fed. Cir. 2011).

Even the *Seagate* test—attacked as overly strict by Petitioners—arguably fails at reserving enhanced damages for rare cases of egregious conduct. Indeed, courts found willfulness in nearly 40% of cases after *Seagate*. Seaman, *Willful Patent Infringement and Enhanced Damages After* In re Seagate: *An Empirical Study*, 97 Iowa L. Rev. 417, 441 (2012). Thus, far from being a rarity, well over a third of cases qualified for enhanced damages even under the rigorous *Seagate* approach. Applying the *Read* factors, courts then awarded enhanced damages in about half of those cases, meaning that one in five cases resulted in an award of enhanced damages. *Id.* at 466. And those awards were usually substantial, with the average total damages award being approximately twice the compensatory damages awarded. *Id.* at 470. Awarding enhanced damages so commonly runs up against the principle that punitive damages must be the exception, not the rule, and should be reserved for extraordinary cases.[5]

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[5] These statistics vary widely across judicial districts. For example, courts found willfulness in over half the cases filed in the Eastern District of Texas, but in only about a quarter of the cases filed in the District of Minnesota. See Seaman, 97 Iowa L. Rev. at 450-451. This emergence of plaintiff-friendly districts militates against weakening the *Seagate* standard and ceding even more discretion to district courts in this sensitive area. Doing so would only increase already-rampant forum-shopping and further cripple the uniform application of the law.

These data offer a compelling argument for further tightening the legal strictures on the award of enhanced damages. At the very least, they strongly caution against weakening those standards. Under the looser pre-*Seagate* test for willfulness, courts awarded enhanced damages twice as often as they do now—in nearly 40% of cases. See Seaman, 97 Iowa L. Rev. at 441, 466.[6] Punitive damages were almost the norm under that legal regime. Any dilution of the *Seagate* standard will lead to the revival of enhanced damages as an everyday occurrence, in direct contravention of this Court's mandate that punitive damages must be rare and reserved for truly outrageous conduct.

II. THE TEST FOR ENHANCED DAMAGES UNDER SECTION 284 SHOULD INCLUDE CONSIDERATIONS AKIN TO THOSE EMPLOYED IN THE PUNITIVE-DAMAGES CONTEXT.

This Court has carefully limited the award of punitive damages outside of the patent context, and many of those legal constraints should be incorporated to restrict the award of enhanced damages under Section 284. In certain respects, Federal Circuit case law already appropriately mirrors this Court's punitive-damages precedents. In determining the test for enhanced damages under Section 284, the goals should be the same as in the punitive-damages context—developing legal doctrines that restrict enhanced damages to rare and egregious cases, provide clear guidance to fact finders, and allow for meaningful appellate review of enhanced-damages awards.

Drawing on punitive-damages doctrine, a proper interpretation of Section 284 will deter extreme cases of

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[6] Before *Seagate*, fact finders found willfulness in 48.2% of cases, and the court awarded enhanced damages in 81.4% of those. Seaman, 97 Iowa L. Rev. at 441, 466.

malicious infringement, such as a competitor delaying or refusing to engage in good-faith licensing negotiations despite a clearly valid patent or a business rival copying a patented innovation without any reasonable basis to do so. But enhanced damages must accomplish that vital task without chilling the aggressive innovation that benefits inventors and consumers alike. This Court's punitive-damages case law offers the legal framework to meet both of these critical objectives.

A. The Federal Circuit's *Seagate* test appropriately draws from this Court's punitive-damages jurisprudence.

1. *The* Seagate *test provides clear guidance to fact finders and predictability to litigants.*

This Court has limited punitive damages to cases "where a defendant's conduct is 'outrageous,' owing to 'gross negligence,' 'willful, wanton, and reckless indifference for the rights of others,' or behavior even more deplorable." *Exxon*, 554 U.S. at 493. The Restatement (Second) of Torts echoes this sentiment: "Punitive damages may be awarded for conduct that is outrageous, because of the defendant's evil motive or his reckless indifference to the rights of others." Restatement (Second) of Torts § 908 (1979). The point is that punitive damages should be awarded only against wrongdoers with significantly heightened culpability.

The Federal Circuit's *Seagate* test imports this requirement into the Section 284 enhanced-damages context. Rather than relying on a vague totality-of-the-circumstances approach, the Federal Circuit in *Seagate* created a strict threshold test to separate those without heightened culpability from those who engaged in the kind of outrageous conduct punitive damages are meant to punish. By requiring both "an objectively high likelihood that [the infringer's] actions constituted infringement of a valid patent" and that that risk "was either

known or so obvious that it should have been known to the accused infringer," the court aligned the enhanced-damages standard with the gross negligence or recklessness threshold employed in the punitive-damages context. *Seagate*, 497 F.3d at 1371. In so doing, it advanced the law closer to ensuring that enhanced damages target "the wanton and malicious pirate" rather than the substantially less culpable "defendant who acted in ignorance or good faith." *Seymour*, 57 U.S. at 488.

This bright-line test goes a long way towards allaying concerns about the "stark unpredictability of punitive awards" as well. *Exxon*, 554 U.S. at 499. The *Seagate* test provides fair notice of when alleged infringers will face the daunting prospect of treble damages and when only compensatory damages (and perhaps attorney's fees) will be at stake. In this way, it honors this Court's mandate that "a penalty should be reasonably predictable in its severity, so that even Justice Holmes's 'bad man' can look ahead with some ability to know what the stakes are in choosing one course of action or another." *Id.* at 502. Predictability is especially important in the patent-infringement context, where an amorphous or overly lenient test for enhanced damages could unduly deter innovators designing products in a field littered with unclear patents.

The *Seagate* test also provides clear legal guidance to fact finders. Fact finders wield great power in awarding punitive damages, whether in a tort case or in an infringement action, and with that power comes the need for "proper legal guidance." *Philip Morris USA* v. *Williams*, 549 U.S. 346, 355 (2007). Indeed, "it is constitutionally important for a court to provide assurance that the jury will ask the right question, not the wrong one." *Ibid.* This need for guidance is particularly acute in the legal labyrinth of infringement actions. In these cases, fact finders must answer complicated factual questions

and apply complex legal standards to unfamiliar and technical facts. See Seaman, 97 Iowa L. Rev. at 451 ("[J]uries made the final decision on willfulness over 70% of the time in the Eastern District of Texas * * * [and] just over half [the time] (54.3%, 144 of 265 cases) elsewhere."). Clear and user-friendly legal tests ease this difficulty and make it more likely that fact finders will "ask the right question." *Philip Morris*, 549 U.S. at 355.

If fact finders are left adrift in a sea of factors and asked to undertake a totality-of-the-circumstances analysis to determine "willfulness" or some other threshold question, they have little chance at arriving at the right question to ask, much less the right answer. In contrast, the *Seagate* test focuses fact finders on specific, concrete issues and thus provides them with the guidance they need to fulfill their role. It also protects defendants from the specter of random or arbitrary fact-finder determinations that could chill good-faith innovators from developing new products and challenging potentially invalid patents. In so doing, this approach provides potential defendants "fair notice * * * of the severity of the penalty that * * * may [be] impose[d]," *Philip Morris*, 549 U.S. at 352 (quoting *BMW of N. Am., Inc.* v. *Gore*, 517 U.S. 559, 574 (1996)), and avoids the constitutional pitfall of "arbitrary punishments," *ibid.* (quoting *State Farm*, 538 U.S. at 416, 418).

2. *Petitioners' alternative test will foster unpredictability for both courts and innovators.*

The *Seagate* test is at the very least a good starting point for bringing enhanced damages law into line with the broader concerns that apply to all types of punitive damages. Stryker takes issue with various aspects of the test, but those criticisms miss the mark.

Stryker's preferred method of determining whether an alleged infringer possesses a "heightened degree of

culpability" is an open-ended, totality-of-the-circumstances test that at times descends into ordinary negligence—asking "whether the defendant continued to infringe after it *knew or reasonably should have known* of the patent" and "whether the defendant, when it *knew or should have known* of the patent, *reasonably* investigated and evaluated the possibility of infringement." Stryker Br. 38 (emphases added). But ordinary negligence cannot be grounds for awarding punitive damages. It certainly has not been under this Court's precedents. See *Exxon*, 554 U.S. at 493 (limiting punitive damages to cases where "a defendant's conduct is 'outrageous,' owing to 'gross negligence,' 'willful, wanton, and reckless indifference for the rights of others,' or behavior even more deplorable"). Thus, Stryker's test violates a core tenet of punitive-damages jurisprudence—that this harsh sanction be reserved for rare cases of egregious conduct.

Stryker's free-flowing inquiry also fails to deliver the predictability required for a punitive-damages test. An unchanneled, holistic standard cannot adequately direct fact finders, much less provide the *ex ante* guidance necessary to inform sound decisionmaking about whether to design or market a new product in a disputed area. The result will be the "stark unpredictability of punitive awards" this Court has sought to avoid. *Id.* at 499.

B. This Court should emphasize the importance of certain punitive-damages factors that protect innovation from both vexatious NPE litigation and egregious trampling of intellectual-property rights.

Federal Circuit case law wisely mirrors this Court's punitive-damages precedents in other respects. The Court should incorporate certain Section 284 factors used by the Federal Circuit and emphasize that these factors must be given great weight in determining whether to award enhanced damages.

After a finding of willfulness under *Seagate*'s threshold test, Federal Circuit precedent requires district courts to consider a number of factors in deciding whether and in what amount to award enhanced damages. *Spectralytics*, 649 F.3d at 1348. As the Federal Circuit has observed, "[u]se of these factors in patent cases is in line with punitive damage considerations in other tort contexts." *Read*, 970 F.2d at 827-828.

1. *Enforcing the "motivation for harm" factor punishes bad-faith infringement by competitors while generally prohibiting enhanced damages for NPEs.*

Whether the defendant had a "motivation for harm," *id.* at 827, is one particularly important factor that district courts should be required to weigh heavily. That factor is reflected in this Court's explanation of the reprehensibility inquiry in punitive-damages cases. As the Court describes it in *State Farm*, whether "the harm was the result of intentional malice, trickery, or deceit" is a key consideration in determining the reprehensibility of the defendant's conduct. 538 U.S. at 419. The absence of those and other indicators of reprehensibility "renders any [punitive-damages] award suspect." *Ibid.*; see also *Chicago Title Ins. Corp.* v. *Magnuson*, 487 F.3d 985, 1001 (6th Cir. 2007) (reversing a $32.4 million punitive-damages award because defendant's "behavior was [not] sufficiently reprehensible for an award of punitive damages").

Emphasizing the importance of a "motivation for harm" is particularly well-suited to the infringement context because it distinguishes between suits by fellow competitors and those by NPEs. A defendant may copy a competitor's product with awareness of the competitor's valid patent to harm the competitor's business and secure a competitive advantage. Or a competitor may delay or refuse to engage in good-faith licensing negotia-

tions despite a patent's clear validity, again with the intention to harm its business rival. Both of these are paradigmatic cases of a defendant with a motivation for harm. Cf. *Wellogix, Inc.* v. *Accenture, L.L.P.*, 716 F.3d 867, 885 (5th Cir. 2013) (upholding punitive damages based on a finding of malicious and reprehensible conduct causing plaintiff's business "value [to] plummet[] when [the competitor-defendant] misappropriated the technology").

In contrast, a defendant who infringes on an NPE's patent rarely has a motivation to harm the NPE. By definition, an NPE is not a competitor in the marketplace, and thus competitive harm is not possible. The infringer may have infringed the NPE's patent by accident, negligence, or even out of a desire to develop products and maximize its own profits despite the existence of the NPE's patent. But, unlike with a fellow competitor, there is no specific motivation to harm the NPE. Thus, this factor will weigh heavily against awarding enhanced damages in NPE cases.

2. *An emphasis on punishing bad-faith copying and refusal to negotiate deters the worst kinds of infringement without unnecessarily arming NPEs with the threat of enhanced damages.*

Two other important considerations that this Court should emphasize are "whether the infringer deliberately copied the ideas or design of another" and "whether the infringer, when he knew of the other's patent protection, investigated the scope of the patent and formed a good-faith belief that it was invalid or that it was not infringed." *Read*, 970 F.2d at 827. These factors translate to the infringement context the reprehensibility consideration of whether the "conduct evinced an indifference to or a reckless disregard of the health or safety of others." *State Farm*, 538 U.S. at 419. Under these factors,

only truly egregious, bad-faith conduct will satisfy the subjective requirement for enhanced damages. Knowingly copying another's validly patented product or delaying or refusing to negotiate for reasonable licensing fees for that product serves no societal value.

Emphasizing these two factors will largely prevent enhanced damages in NPE cases. NPEs do not have products, which makes it nearly impossible for an infringer to deliberately copy an NPE's idea or design. Only the egregious case of an infringer discovering an NPE's patent and then directly copying the idea would typically satisfy that factor.

Additionally, NPEs, unlike operating companies, rarely give notice of the alleged infringement before filing suit. See Love, *An Empirical Study of Patent Litigation Timing: Could A Patent Term Reduction Decimate Trolls Without Harming Innovators?*, 161 U. Pa. L. Rev. 1309, 1354 (2013). That is because NPEs place a high priority on obtaining venue in one of their favored judicial districts. They dare not risk tipping off an alleged infringer for fear that he will file a declaratory judgment action in some other district before the NPE can file suit. See *ibid.* Thus, in the vast majority of NPE cases the moment "when [the alleged infringer] knew of the other's patent protection" is the same time the NPE filed suit. *Read*, 970 F.2d at 827. And if the relevant time period is when litigation commences, an alleged infringer will nearly always either "investigate[] the scope of the patent and form[] a good-faith belief that it was invalid or that it was not infringed" or else settle the case if he realizes he possesses no colorable defense. *Ibid.* Consequently, this important consideration in awarding enhanced damages will almost always be absent from NPE cases.

The common scenario in NPE litigation described above also refutes the Government's concerns with the

Federal Circuit's objective threshold for willfulness, which bars enhanced damages so long as the defendant presents objectively reasonable defenses at trial. The Government urges that any test of objective reasonableness must measure only the legal defenses of which the defendant was aware at the time of the allegedly willful infringement, not at the time of trial. United States Br. 25, 29-31. In the NPE scenario described above, however, these two timeframes converge: The defendant becomes aware of possible infringement at essentially the same time that litigation commences, and the defendant is only then able to develop his defenses for the first time. Thus, there is no possibility of post-hoc rationalizations shielding bad-faith behavior in the typical NPE case. As a result, the Government's attack on the Federal Circuit's objective test is a red herring in the context of much NPE litigation—which now constitutes over two-thirds of all patent litigation.[7]

3. *These punitive-damages considerations protect against unfair competition while limiting the* in terrorem *effect of NPE lawsuits.*

By requiring district courts to scrutinize the three factors discussed above, the Court would meaningfully differentiate between competitor and NPE lawsuits. This would alleviate the worst chilling effects that enhanced damages can have on innovation. More and more, those who invest the billions of dollars required to develop new products must pay a steep and ever-rising tax to NPEs who engage in no creative activity whatsoever. Costs to defend and resolve NPE suits have increased 18% per

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[7] RPX Corp., 2015 NPE Activity: Highlights 4 (2016), https://www.rpxcorp.com/wp-content/uploads/sites/2/2016/01/RPX-2015-NPE-Activity-Highlights-FinalZ.pdf.

year on average from 2009 to 2014.[8] And in 2014 alone, companies spent more than $12 billion to resolve NPE patent disputes.[9] This disturbing trend has been accompanied by an alarming rise in NPE activity, which grew from 640 cases filed in 2009 to 2,791 cases filed in 2014.[10] The problem is real, and it continues to grow.

A company faced with an NPE suit has only bad options. It can spend huge sums of money defending the case and risk a potentially large adverse verdict or it can pay the ransom and settle the perhaps borderline-frivolous case. Members of this Court have expressed their concern about "increas[ing] the *in terrorem* power of patent trolls," and for good reason. *Commil USA, LLC* v. *Cisco Sys., Inc.*, 135 S. Ct. 1920, 1932 (2015) (Scalia, J., dissenting). But granting NPEs easier access to the awesome power of treble damages would do just that. Fewer companies will be willing to risk going to trial against NPEs if the prospect of commonly available treble damages is hanging over them. Many more will choose the path of least resistance.

As importantly, rational companies must weigh the projected costs of infringement suits, and particularly the all-too-common NPE suits, against the potential revenue of a new product. Each increase in those costs—and especially the substantial increase that would result from easing the restraints on treble damages—means that fewer innovations will be worth the considerable trouble of inventing.

At the same time, enhanced damages play an indispensable role in patent law. Without enhanced damages,

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[8] RPX Corp., 2014 NPE Cost Report: High-level Findings 10 (2015), https://www.rpxcorp.com/wp-content/uploads/sites/2/2015/05/RPX-2014-NPE-Cost-Report-ZZFinal.pdf.

[9] *Ibid.*

[10] *Ibid.*

a would-be infringer has little to lose by deliberating copying a patented product and refusing overtures to negotiate a reasonable royalty. Even if the infringer loses in litigation, the damages will be only the royalty it would have otherwise paid. Yet the patent holder will suffer not only litigation expenses, but often irreparable harm to its business. Enhanced damages exist to deter this particularly harmful type of willful infringement that brazenly disrespects a patent holder's intellectual property rights without any legal basis to do so. This core function of enhanced damages must be preserved.

By elevating the importance of these three punitive-damages considerations that allow treble damages against competitors in appropriate instances—but almost always prohibit them in NPE cases—the Court can eliminate the bulk of the chilling effects that treble damages have on beneficial innovation while also maintaining them as a strong deterrent against the worst types of infringement.

C. As with punitive damages, courts should award enhanced damages only when necessary to deter future wrongdoing.

1. *Enhanced damages must deter flagrant disregard of intellectual property rights without discouraging challenges to patents generally.*

The centrality of deterrence to punitive-damages awards should apply equally to enhanced-damages awards under Section 284. This Court's punitive-damages cases uniformly hold that deterrence is a principal aim of punitive damages. See *Exxon*, 554 U.S. at 492 ("[P]unitives are aimed * * * principally at retribution and deterring harmful conduct."); *Cooper*, 532 U.S. at 432 (punitive damages are "intended to punish the defendant and to deter future wrongdoing"). Indeed, "punitive damages should *only* be awarded if the defendant's

culpability, after having paid compensatory damages, is so reprehensible as to warrant the imposition of further sanctions to achieve punishment or deterrence." *State Farm*, 538 U.S. at 419 (emphasis added).

Achieving the appropriate level of deterrence is all the more crucial in the patent-infringement arena. The consequences of over-deterrence in this area are especially severe—the chilling of innovation. After all, "good faith challenges to the validity or scope of patent rights should be encouraged rather than punished" because they help police the system and enable further innovation. 7 Chisum on Patents § 20.03[4][b][iii] (2009). Given these countervailing considerations, the harsh sanction of enhanced damages must be wielded reluctantly and only in the face of egregious conduct.

Compensatory damages and the steep cost of litigation already deter much infringing behavior. Indeed, those considerations have prompted companies like Huawei to engage in a rigorous (and expensive) review of similar technologies and any corresponding patents before proceeding with developing a new invention. See *Mayo Collaborative Servs.* v. *Prometheus Labs., Inc.*, 132 S. Ct. 1289, 1305 (2012) (recognizing that innovators must conduct "costly and time-consuming searches of existing patents and pending patent applications"). That task often proves futile or overwhelming given the sheer volume of material and the constraints of time and cost. For example, in the software industry, "[e]ven if a patent lawyer only needed to look at a patent for ten minutes, on average, to determine whether any part of a particular firm's software infringed it, it would require roughly two million patent attorneys, working full-time, to compare every firm's products with every patent." Mulligan & Lee, *Scaling the Patent System*, 68 N.Y.U. Ann. Surv. Am. L. 289, 304-305 (2012). Given the deterrent effect already in evidence, making enhanced damages more widely availa-

ble is unnecessary and would only exacerbate the burdens borne by innovators.

That is not to say that enhanced damages have no deterrent role to play in certain cases. These punitive damages should only be awarded to deter truly outrageous conduct, such as deliberately copying a competitor's patented product or delaying or refusing to engage in good-faith licensing negotiations despite full knowledge of the valid patent. An infringer who takes those extreme steps, either out of bad faith or indifferent recklessness, requires additional deterrence beyond the compensatory damages and litigation costs that are sufficient in the vast majority of cases. That is the proper place to deploy the rare sanction of enhanced damages. The standard for awarding enhanced damages must therefore precisely differentiate between ordinary infringement and egregious conduct requiring additional deterrence.

2. *Deterrence rarely justifies awarding enhanced damages in NPE cases.*

The deterrent purpose of punitive damages largely rules out enhanced damages for NPEs. A would-be infringer of an NPE's patent stands to gain only the licensing fees it would have otherwise paid, whereas a would-be infringer of a competitor's patent avoids licensing fees *and gains increased market share* by providing those patented products at a lower price. The greater the potential reward, the greater the deterrent must be.[11] Thus, enhanced damages serve an appropriate deterrent function primarily in suits by competitors—not NPEs.

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[11] It is worth noting that the median damages award in NPE cases is currently over four times that in non-NPE cases. PricewaterhouseCoopers LLP, 2015 Patent Litigation Study 4 (May 2015), http://www.pwc.com/us/en/forensic-services/publications/assets/2015-pwc-patent-litigation-study.pdf. Accepting Petitioners' invitation to lower the bar for enhanced damages would thus result in further windfalls to NPEs untethered to any reasonable need for deterrence.

Equitable considerations support this approach as well. An NPE typically makes its money on licensing fees, not by making a better product or providing better services. Thus, infringement causes an NPE to lose only those licensing fees. Compensatory damages (and perhaps attorney's fees in "exceptional" cases) will make the NPE whole. By contrast, these traditional damages may not be able to capture the irreparable harm that a pirated product can do to a competitor's business. Thus, some form of additional damages may be necessary to deter in this latter situation, but clearly not in the former.

D. Enhanced damages, like punitive damages, must be subject to searching appellate review.

This Court should require rigorous appellate review of enhanced-damages awards, just as it has for punitive-damages awards more generally. In a punitive-damages case, the court conducts an evidentiary-sufficiency review of the jury's threshold findings that make the case eligible for punitive damages and then reviews de novo the district court's application of the constitutional factors that limit the availability and amount of punitive damages. See, *e.g.*, *Wellogix*, 716 F.3d at 883-884. The Federal Circuit, too, currently reviews the different determinations underpinning an award of enhanced damages with varying degrees of deference. The first prong of the *Seagate* test, which focuses on the objective risk of infringement, is reviewed de novo. *Bard Peripheral Vascular, Inc.* v. *W.L. Gore & Assocs., Inc.*, 682 F.3d 1003, 1008 (Fed. Cir. 2012). The second prong of that test, which asks whether the defendant knew or should have known of that risk, is reviewed for substantial evidence. *Ibid.* Then, the district court's decision of whether and in what amount to award enhanced damages under the *Read* factors is reviewed for abuse of discretion. *Spectralytics*, 649 F.3d at 1347.

The standards of review for the two prongs of the *Seagate* test stem from their legal and factual nature, respectively. Because the assessment of whether there is an objectively high risk of infringement is a question of law, it must be reviewed de novo. *Bard*, 682 F.3d at 1006-1007. Indeed, that question often comes down to an "objective assessment"—"whether a 'reasonable litigant could realistically expect' those defenses to succeed." *Id.* at 1006, 1008. The relative strength or weakness of legal defenses is an issue for judges, not juries. Likewise, because whether the defendant knew or should have known about the infringement risk is a question of fact, it must be reviewed for substantial evidence. *Id.* at 1008.

Abuse-of-discretion review of the district court's ultimate decision to award enhanced damages is more troubling. In the broader punitive-damages context, this Court has stressed the need for "[e]xacting appellate review" of punitive-damages awards. *State Farm*, 538 U.S. at 418. While that exacting review may be possible with a particularly rigorous abuse-of-discretion analysis focusing heavily on the legal conclusions underlying the award of enhanced damages, a de novo standard of review accomplishes this goal much more naturally. Indeed, "courts of appeals should apply a de novo standard of review when passing on district courts' determinations of the constitutionality of punitive damages awards." *Cooper*, 532 U.S. at 436. That de novo standard should govern a district court's assessment of enhanced damages under Section 284 as well. The same need for careful review of a powerful remedy exists here.

Rigorous appellate review is arguably even more important in patent cases because NPEs tend to file suit in districts "perceived as favorable" to plaintiffs. See Seaman, 97 Iowa L. Rev. at 449; see also Leychkis, *Of Fire Ants and Claim Construction: An Empirical Study of the Meteoric Rise of the Eastern District of Texas As A*

Preeminent Forum for Patent Litigation, 9 Yale J.L. & Tech. 193, 206 (2007) ("Plaintiff patent holders and their attorneys love the Eastern District of Texas."). De novo review of these awards would ensure uniform application of the law, which is essential to cabin this powerful punitive measure and neutralize forum-shopping by litigants.

CONCLUSION

Huawei respectfully requests that the judgments of the Court of Appeals be affirmed.

Respectfully submitted.

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